

Analyst: Paul Sham

DAH SING FINANCIAL HOLDINGS LIMITED (大新金融)

Sector	: Banking	Chairman	: Mr. David Shou-Yeh Wong
HKSE Code	: 00440		
Market Price	: HK\$46.70 (24/03/2011)	Managing Director & Chief Executive	: Mr. Derek Hon-Hing Wong
Shares Issued	: 292.8m		
Mkt. Cap.	: HK\$13,673.8m		
52 weeks Hi/ Lo	: HK\$63.22 / HK\$35.60		
HSI	: 22,915.28 (24/03/2011)		
Main Business	: Banking and related financial services		

SUMMARY OF THE FINAL RESULTS FOR THE YEAR ENDED 31ST DECEMBER 2010

Final Results Highlights

	HK\$ million	Vs FY2009 (%)	Vs 30/06/2010 (%)
• Net interest income	2,179.5	-7.0%	
• Non-interest income	613.0	+61.4%	
• Total operating income	2,792.5	+2.5%	
• Operating expenses	(1,454.0)	-22.2%	
• Operating profit before impairment losses	1,338.6	+56.6%	
• Impairment losses on loans and advances	(97.8)	-123.9%	
• Profit before taxation	1,499.1	+69.3%	
• Taxation	(214.0)	+122.4%	
• Attributable profit to shareholders	1,006.3	+60.7%	
• Total loans	72,749.0	+27.3%	+11.6%
• Total deposits	100,872.7	+11.5%	+10.5%
• Total assets	142,741.5	+16.5%	+11.5%
• Basic EPS (HK\$)	3.67	+52.3%	
• Final DPS (HK\$)	0.86	NA*	
• Total DPS (HK\$)	1.06	NA*	
Selected Ratios	FY2010	FY2009	1H2010
• Net interest margin	1.68%	1.95%	1.87%
• Cost-income ratio	52.1%	68.6%	51.6%
• Return on average assets	0.80%	0.50%	0.80%
• Return on average equity	7.90%	5.90%	8.60%
• Impaired loan ratio	0.25%	0.96%	0.53%
• Impaired advances coverage	216.9%	123.4%	162.0%
• Loan-deposit ratio	72.1%	63.2%	71.4%
• Capital adequacy ratio	16.3%	16.8%	17.2%
• Average liquidity ratio	45.7%	57.3%	48.6%

Remarks: (*)DSF did not propose dividend in FY09

- **Core earnings were disappointing in FY10** Dah Sing Financial (DSF) reported a fair set of results in FY10. Attributable profit rose 60.7% y-o-y to HK\$1,006.3m and was in-line with market consensus of HK\$1,008.8m. Core earnings were a bit disappointing on weak interest income and modest growth in fee income. Positives were seen in trading gains, lower impairment losses and rising contribution from Bank of Chongqing (BOCQ). DSF resumed dividend payments in FY10, following dividend suspension since 2H08. With final dividend per share of HK\$0.86, total dividend per share in FY10 amounted to HK\$1.06, representing payout ratio of 28.9%.

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- **DAH SING BANKING GROUP (DSB#2356) net profit disappointed the market** DSB's 74.1%-owned banking arm DSB posted a 78.8% increase in net profit to HK\$1,074.1m, also in-line with the market estimate.

	HK\$ million	Vs FY2009 (%)	Vs 30/06/2010 (%)
• Net interest income	1,955.5	-8.4%	
• Non-interest income	470.1	+133.6%	
• Total operating income	2,425.7	+3.8%	
• Operating expenses	(1,278.4)	-25.9%	
• Operating profit before impairment losses	1,147.3	+88.1%	
• Impairment losses on loans and advances	(97.8)	-77.1%	
• Profit before taxation	1,267.6	+85.4%	
• Taxation	(193.5)	+133.8%	
• Attributable profit to shareholders	1,074.1	+78.8%	
• Total loans	72,749.0	+27.3%	+11.6%
• Total deposits	102,027.0	+11.3%	+10.2%
• Total assets	131,838.7	+16.0%	+11.2%
• Basic EPS (HK\$)	0.92	+53.3%	
• Final DPS (HK\$)	0.20	NA*	
• Total DPS (HK\$)	0.27	NA*	

Selected Ratios	FY2010	FY2009	1H2010
• Net interest margin	1.68%	1.95%	1.87%
• Cost-income ratio	52.7%	73.9%	54.4%
• Return on average assets	0.90%	0.50%	0.90%
• Return on average equity	8.80%	6.30%	9.10%
• Impaired loan ratio	0.25%	0.96%	0.53%
• Impaired advances coverage	216.9%	123.4%	162.0%
• Loan-deposit ratio	71.3%	62.4%	70.4%
• Capital adequacy ratio	16.3%	16.8%	17.2%
• Average liquidity ratio	45.7%	57.3%	48.6%

Remarks: (*)DSB did not propose dividend in FY09

- Net interest income contracted by 8.4% during 2010. DSB's net interest margin declined sharply to 1.68% in FY10, compared with 1.87% a year earlier, mainly due to lower loan yield and lower return on surplus fund. Nevertheless, strong loan growth helped offset the weakness in margins. During FY10, DSB's loan book expanded by 27.3%, driven by lending in property (+27.4%) and loan outside HK (+48.3%). Deposits were up only 11.3% y-o-y which lifted the loan-to-deposit ratio to 71.3% at end-2010.
- Non-interest income increased by 133.6% y-o-y. Net fee income rose modestly by 11% in 2010, with credit card fees and brokerage fees, the two main contributors to the net fee income, growing 20% and 6.9% respectively. Nevertheless, the actual driving force behind the non-interest income in 2010 was the trading income, which improved substantially from a net loss of HK\$175m in FY09 to a profit of HK\$50m in FY10.
- Operating expenses recorded a significant decline in FY10, down 25.9% y-o-y, mainly due to the absence of further provision charges relating to the repurchases of Lehman Brothers Minibonds. Salary expenses, the largest contributor of operating expenses, increased by 9.3% in FY10. Cost-to-income ratio fell from FY09's peak of 71.3% to 52.5% in FY10. However, it was still higher than the average level of 40% during FY06 and FY07 as expenditure for business development in China increased.
- Loan impairment charges dropped 77.1% y-o-y as a result of the improved economic conditions. NPL ratio also improved notably to 0.25% versus 0.96% at the end of 2009.
- DSB raised HK\$1bn via a rights issue in November 2010. The capital raised was not included in the CAR ratio in FY10 as the funds were yet to be deployed. Management estimated that core and total CAR would be 11.3% and 17.5% if the fund was included, higher than the stated 10.2% and 16.3%, respectively.

- **Insurance business helped by investment gains** DSF's life business reported a 30% y-o-y increase in net profit, principally due to higher investment income and increases in the embedded value of in-force life policies, which more than offset the increases in insurance claims and reserves. Nevertheless, DSF's agency force declined to fewer than 400 agents currently due to the strong agency competition in local insurance industry.

Outlook & Prospects

- **2011 interest income outlook** Management disclosed during analyst briefing that net interest margin will likely further narrow to 1.5% to 1.6%. The fierce competition for deposits in the domestic market will place upward pressure on funding costs while sustained low interest rates will remain a drag on return from treasury operations and return on free funds. Given the uncertain timing when US interest rates will rise in the future, only a single-digit or even negative growth in net interest income should be expected this year.
- **Insurance business as a swinging factor** Although sluggish top-line growth was seen in FY10, DSF's life business still posted a strong bottom-line earnings which was helped by strong investment income. In contrast, DSF recorded losses in FY08 amid poor investment return despite healthy top-line growth. Therefore, we believe the profitability of DSF's insurance segment in FY11, which will be largely determined by its investment performance, will lead to a big swinging factor for DSF's overall earnings.
- **Listing of BOCQ** Net profit from BOCQ rose 27% y-o-y in FY10 and accounted for about 20% of DSF's total net profit. Investors are expecting the listing of BOCQ could be a big catalyst for DSF's share prices. Nevertheless, Management admitted that BOCQ's A-share listing would not occur by 1H12 as it is pending approval from China Securities Regulatory Commission and there is still a long queue of mainland banks waiting to conduct IPOs.
- **Lack of catalyst but undemanding valuations** DSF is characterized by its low profitability, relatively insignificant China exposure and weak franchise/growth prospects in HK banking operations. While the weaker NIM and lacklustre insurance-premium growth for 2010 were disappointing, the downside risk for DSF should be limited, as it is currently trading at 0.92x book, the lowest level in the past 10 years. With a return of M&A theme to the HK banking sector following the privatization of ICBC(Asia) and Fubon(HK), DSF is very likely to be the next acquisition target. As such, we recommend a "buy on weakness" on the counter.

Recommendation: Buy on weakness

I. Impairment allowances, overdue and rescheduled advances of Dah Sing Financial

As % of total customer advances	Individual allowance	Portfolio allowance	Non-performing loans	Overdue and rescheduled advances
As of 31/12/2010	0.13%	0.42%	0.25%	0.56%
As of 30/6/2010	0.31%	0.55%	0.53%	0.34%
As of 31/12/2009	0.55%	0.63%	0.96%	1.38%

II. Comparison of Dah Sing Financial's loan book: 31/12/2010 vs 31/12/2009

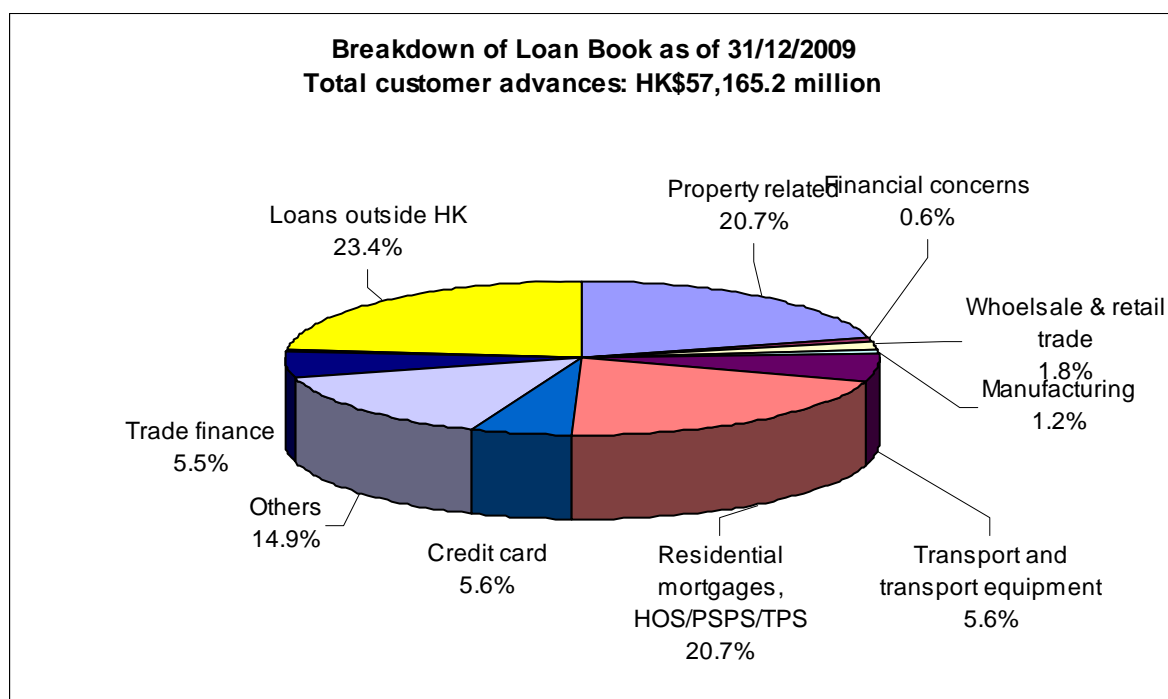
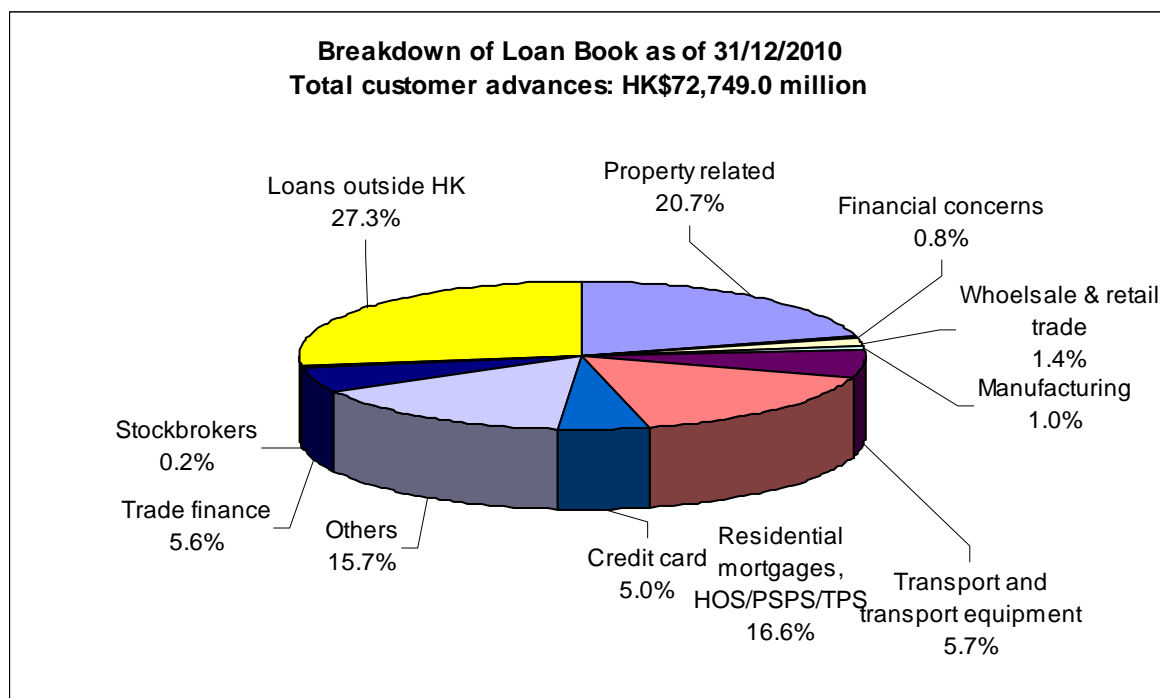
Loans-by industry	31 st Dec, 2010 HK\$ million	Up/(down)	31 st Dec, 2009 HK\$ million
Property related	15,064.1	+27.4%	11,820.2
Financial concerns	596.3	+78.9%	333.2
Wholesale & retail trade	1,026.1	+2.5%	1,001.2
Manufacturing	725.3	+10.3%	657.6
Transport & transport equipment	4,173.4	+30.1%	3,207.3
Residential mortgages, HOS/PSPS	12,055.2	+1.6%	11,860.5
Credit card	3,654.6	+15.2%	3,173.6
Others	11,413.4	+34.0%	8,517.3
Trade finance	4,042.4	+28.9%	3,136.8
Stockbrokers	116.1	+122.2%	52.3
Loans outside HK	19,882.1	+48.3%	13,405.1
	<u>72,749.0</u>	<u>+27.3%</u>	<u>57,165.2</u>

III. Comparison of Dah Sing Financial's loan book: 31/12/2010 vs 30/06/2010

Loans-by industry	31 st Dec, 2010 HK\$ million	Up/(down)	30 th Jun, 2010 HK\$ million
Property related	15,064.1	+11.9%	13,459.3
Financial concerns	596.3	+17.0%	509.9
Wholesale & retail trade	1,026.1	+7.3%	956.1
Manufacturing	725.3	-6.3%	773.8
Transport & transport equipment	4,173.4	+15.6%	3,611.4
Residential mortgages, HOS/PSPS	12,055.2	-2.2%	12,323.0
Credit card	3,654.6	+13.4%	3,223.9
Others	11,413.4	+11.8%	10,209.5
Trade finance	4,042.4	+2.9%	3,928.7
Stockbrokers	116.1	+71.5%	67.7
Loans outside HK	19,882.1	+23.1%	16,147.8
	<u>72,749.0</u>	<u>+11.6%</u>	<u>65,210.9</u>



Breakdown of loan book of Dah Sing Financial



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